



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
1100 Commerce Street, MC 4920 DAL
Dallas, TX 75242

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date NOV 30 2016

Release Number: **201710031**
Release Date: 3/10/2017
UIL Code: 501.03-00

Person to Contact:

Identification Number:

Contact Telephone Number:

Telephone Number:

Fax:

EIN:

CERTIFIED MAIL - Return Receipt Requested

Dear :

This is a final determination that your exempt status under section 501(c)(3) of the Internal Revenue Code is revoked. The recognition of your exemption under Internal Revenue Code section 501(c)(3) is revoked effective as of January 1, 20XX for the following reason(s):

You have failed to demonstrate that you are operated exclusively for exempt purposes within the meaning of section 501(c)(3) of the Internal Revenue Code, as a substantial part of your operations are to further non-exempt purposes. You have also failed to demonstrate that your operations meet the requirements of section 509(a)(2) of the Internal Revenue Code, as your primary source of support is rental income.

Contributions to your organization are no longer deductible under section 170 of the Internal Revenue Code effective as of January 1, 20XX.

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the year ending December 31, 20XX, and for all subsequent years.

Processing of income tax returns and assessment of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination in court, you must initiate a suit for declaratory judgment in the United States Tax Court, the United States Claim Court or the District Court of the United States for the District of Columbia before the 91st day after the date this determination was mailed to you. Contact the clerk of the appropriate court for the rules for initiating suits for declaratory judgment. Please contact the clerk of the respective court for rules and the appropriate forms regarding filing petitions for declaratory judgment by referring to the enclosed Publication 892. Please note that the United States Tax Court is the only one of these courts where a declaratory judgment action can be pursued without the services of a lawyer. You may write to the courts at the following addresses:

United States Tax Court
400 Second Street, NW
Washington, DC 20217

US Court of Federal Claims
717 Madison Place, NW
Washington, DC 20005

U. S. District Court for the District of Columbia
333 Constitution Ave., N.W.
Washington, DC 20001

You may call the IRS telephone number listed in your local directory. An IRS employee there may be able to help you, but the contact person at the address shown on this letter is most familiar with your case. You may also call the Internal Revenue Service Taxpayer Advocate.

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. We can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for our assistance, which is always free, we will do everything possible to help you. Visit taxpayeradvocate.irs.gov or call 1-877-777-4778.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours,

Enclosures:
Publication 892
Envelope

for
Mary A. Epps
Acting Director, EO Examinations



**Department of the Treasury
Internal Revenue Service
Tax Exempt and Government Entities
Exempt Organizations Examinations**

Date: May 12, 2016

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

December 31, 20XX and 20XX

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Manager's Name/ID Number:

Manager's Contact Number:

Response due date: June 11, 20XX

Certified Mail – Return Receipt Requested

Dear :

Why you are receiving this letter

We propose to revoke your status as an organization described in section 501(c)(3) of the Internal Revenue Code (Code). Enclosed is our report of examination explaining the proposed action.

What you need to do if you agree

If you agree with our proposal, please sign the enclosed Form 6018, *Consent to Proposed Action – Section 7428*, and return it to the contact person at the address listed above (unless you have already provided us a signed Form 6018). We'll issue a final revocation letter determining that you aren't an organization described in section 501(c)(3).

After we issue the final revocation letter, we'll announce that your organization is no longer eligible for contributions deductible under section 170 of the Code.

If we don't hear from you

If you don't respond to this proposal within 30 calendar days from the date of this letter, we'll issue a final revocation letter. Failing to respond to this proposal will adversely impact your legal standing to seek a declaratory judgment because you failed to exhaust your administrative remedies.

Effect of revocation status

If you receive a final revocation letter, you'll be required to file federal income tax returns for the tax year(s) shown above as well as for subsequent tax years.

What you need to do if you disagree with the proposed revocation

If you disagree with our proposed revocation, you may request a meeting or telephone conference with the supervisor of the IRS contact identified in the heading of this letter. You also may file a protest with the IRS Appeals office by submitting a written request to the contact person at the address listed above within 30 calendar days from the date of this letter. The Appeals office is independent of the Exempt Organizations division and resolves most disputes informally.

For your protest to be valid, it must contain certain specific information including a statement of the facts, the applicable law, and arguments in support of your position. For specific information needed for a valid protest, please refer to page one of the enclosed Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*, and page six of the enclosed Publication 3498, *The Examination Process*. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process. Please note that Fast Track Mediation referred to in Publication 3498 generally doesn't apply after we issue this letter.

You also may request that we refer this matter for technical advice as explained in Publication 892. Please contact the individual identified on the first page of this letter if you are considering requesting technical advice. If we issue a determination letter to you based on a technical advice memorandum issued by the Exempt Organizations Rulings and Agreements office, no further IRS administrative appeal will be available to you.

Contacting the Taxpayer Advocate Office is a taxpayer right

You have the right to contact the office of the Taxpayer Advocate. Their assistance isn't a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate can't reverse a legally correct tax determination or extend the time you have (fixed by law) to file a petition in a United States court. They can, however, see that a tax matter that hasn't been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Internal Revenue Service
Office of the Taxpayer Advocate

For additional information

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Paul A. Marmolejo
Acting Director, EO Examinations

Enclosures:
Report of Examination
Form 6018
Publication 892
Publication 3498

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 1 of 14
Name of Taxpayer		Year Ended December 31, 20XX

ISSUES:

1. Whether (the EO) qualified for exemption under IRC Section 501(c)(3) during the year of examination?
2. Whether the EO's exemption under IRC 501(c)(3), further described in IRC Section 509(a)(2), should be revoked effective January 1, 20XX.

FACTS:

Background Information

, ("EO", Exempt Organization), was granted exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code. It was further described in section 509(a)(2), as a publicly supported organization in determination Letter 391 dated 02-09-19XX. The EO provided an updated Tax Exemption Letter dated 11-14-20XX. The organization was exempt under Section 501(c)(3) and classified as a public charity under Section 509(a)(2) of the Internal Revenue Code.

The EO filed with the IRS Form 1023, *Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code* on 11-05-19XX.

The Declaration of Trust (**the Trust**) Creating , dated 01-10-19XX, was filed for record in the Misc. Deed Records of Volume XX, Page XXX.

The Trust was created exclusively for public, charitable and educational purposes; "

".

The Declaration of Trust had VIII Parts:

I. Trustees and Officers

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 2 of 14
Name of Taxpayer		Year Ended December 31, 20XX

- II. Method of Action by Trustees
- III. Powers of Trustees
- IV. Purposes of the Trust
- V. Restrictions and Limitations
- VI. Fiscal Year
- VII Revocation and Alterations
- VII Execution

Part IV stated, in part, the **"Purpose of the Trust"**: *"This Trust is created exclusively for public charitable and educational purposes, as herein defined, as made more specific in the next following paragraph. The term "public charitable and educational purposes" as used herein shall have the broadest signification accorded to it by the Courts, within the limits of the rule sanctioning the creation of trusts in perpetuity for public charitable and educational purposes, and also within such Limits as are now or hereafter may be imposed by the United States Internal Revenue Code in recognizing the deductible character and non-taxability of gifts for charitable and educational purposes and the non-taxability of income to and from charitable and educational foundations."*

Part V stated, in part, the **"Restrictions and Limitations"**:

2) *"The following provision shall be applicable to the Trust Estate, to-wit:*

- (a) *The trust property, including corpus and accumulated income, shall be used only within the United States or its possessions exclusively for public charitable and educational purposes.*
- (b) *No part of the net earnings of the Foundation shall inure to the benefit of any private shareholder or individual.*
- (c) *No substantial part of the activities of the Foundation shall be carrying on propaganda or otherwise attempting to influence legislation. The Foundation shall not participate in, or intervene in (including the publishing or distributing of statements), or any political campaign on behalf of any candidate for public office.*
- (d) *No officer, member or employee of the Foundation shall receive any pecuniary profit from the operation thereof, except reasonable compensation for services rendered in effecting one or more purposes of the Foundation.*

3) *The Foundation shall not:*

- (a) *Lend any part of its income or corpus without the receipt of adequate security and a reasonable rate of interest, to;*

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 3 of 14
Name of Taxpayer		Year Ended December 31, 20XX

- (b) Pay any compensation in excess of a reasonable allowance for salaries or other compensation for personal services actually rendered, to;*
- (c) Make any part of its services available on a preferential basis, to;*
- (d) Make any substantial purchases of securities or any other property for more than adequate consideration in money or money's worth, from;*
- (e) Sell any substantial part of its securities or other property for less than an adequate consideration in money or money's worth, to;*
- (f) Engage in any other transaction which results in a substantial divergence of its income or corpus, to; any person who has made a substantial contribution to the Foundation, any member of the family (as defined in the applicable provisions of the Internal Revenue Code) of such an individual, or any corporation in which any person whose has made a substantial contribution to the Foundation owns, directly or indirectly, fifty per centum or more of the total combined voting power of all classes of stock entitled to vote, or fifty per centum or more of the total value of shares of all classes of stock of the corporation.*
- (g) Accumulate out of income an amount which is unreasonable in size or which is retained for an unreasonable length of time.*
- (h) Invest any amount accumulated out of income in such a manner as to jeopardize the carrying out of the purposes of the Foundation which constitute a basis for exemption under the applicable provisions of the Internal Revenue Code.*

4) The trust property or any part thereof may, at the direction of the Trustees, be distributed to any scientific, educational, literary, or charitable corporation, trust, fund or foundation, no part of the earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), or any political campaign on behalf any candidate for public office; provided further that distributions to a trust fund or foundation are to be used exclusively within the United States or its possessions."

Part VII stated the "Revocation and Alteration":

"The trust shall be irrevocable. In the event the Foundation does not qualify as an organization exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code of 1954 or the corresponding section of any subsequent Revenue Act, then the Board, acting by and through its duly elected Board of Directors, shall have the power to alter or amend the Trust, but only to the extent necessary to qualify the Foundation as an exempt organization under such Section. Any such alteration or amendment shall be by instrument in writing delivered to the Trustees and by them duly adopted. In

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 4 of 14
Name of Taxpayer		Year Ended December 31, 20XX

the event, but only in the event, that the trust herein created shall be held by a final decree of a court of competent jurisdiction to be within the rule against perpetuities, the foregoing grant to the Trust Estate and any additional grant or grants shall be for a term ending twenty-one years after the death of the last to survive of the original Trustees hereinabove named, the same as if such grant or grants had been expressly made for such limited term, and at the expiration of such period the Trustees shall distribute the whole of the Trust Estate then remaining to such non-profit, permanent educational institutions as they may determine to be in the best position to carry out and subserve the original purposes of the Foundation, whereupon this trust shall terminate.

The EO provided a copy of its Articles of Incorporation filed with the Secretary of the State of on August 19, 19XX. The new name of the organization was

The EO provided a copy of its By-Laws dated August 25, 19XX. The name of the organization appears as

The Admin File was requested and obtained from the Records Unit, but no copy of the Articles of Incorporation or By-Laws were included.

The Office of the of the State of revoked the EO's exemption under Section of the Statute as of January 10, 20XX. The reason was that the EO did not provide an updated Determination Letter (After the Incorporation in 19XX) from the IRS. The EO provided to the Comptroller the IRS Determination Letter that indicated that the Federal exemption was granted to the *unincorporated entity*, the and not the

The EO filed a Final Return by check marking "Terminated" on its Form 990 for the year beginning 01-01-20XX and ending in 08-31-20XX. The return was dated 06-20-20XX and filed on time.

The Audit

The Form 990 for the year ending 12-31-20XX stated the EO's mission as "The Trust was created exclusively for public charitable and educational purposes".

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 5 of 14
Name of Taxpayer		Year Ended December 31, 20XX

Present at the interview were _____ (the **POA** and CPA) and _____, (the **Bookkeeper**). The interview and review of the books and records took place at the CPA's office as the EO did not have a place to conduct business.

The POA stated that the _____ had terminated its activities on 08-31-20XX, which was the subsequent year of this examination.

Public Support Test

The EO did not pass the Public Support Test. The EO failed to be a 509(a)(2) publicly supported organization as they received **less** than one-third support from gifts, grants, contributions, membership fees, and certain gross receipts. The EO received **more** than one-third support from net unrelated business taxable income.

The EO's total income was coming from \$XX in donations and \$XX,XXX from rental income. No other income was found. The total income was XX,XXX, making rental income, an unrelated business income, XX percent of the total support. It was a similar situation in the subsequent year.

The organization was not a 501(c)(3) further described in IRC Section 509(a)(2) as it failed the Public Support Test.

IRC Section 509(a)(2) organizations are supported primarily by exempt function income. Exempt function income is described as funds derived from an activity which is not an unrelated trade or business.

Organizations qualifying under **Section 509(a)(2)** normally receive not more than one-third of its support from gross investment income and more than one-third of its support from contributions, membership fees, and gross receipts from activities related to its exempt functions (subject to certain exceptions).

An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Dual Test: Organizational and Operational Test.

The EO did not satisfy the Dual Test.

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 6 of 14
Name of Taxpayer		Year Ended December 31, 20XX

IRC 501(c)(3) requires an organization to be both "organized and operated" exclusively for one or more IRC 501(c)(3) purpose. If the Organization fails either the organizational test or the operational test, it is not exempt. *Reg. 1.501(c)(3)-1(a)(1).*

Organizational Test

The EO passed the Organizational Test.

- 1) Reg. 1.501(c)(3)-1(b)(1)(i) provide that an origination is organized exclusively for one of more exempt purposes only if its articles of organization:
 - Limit the purposes of such organization to one or more exempt purposes; and
 - Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.
- 2) In addition, the organization's assets must be dedicated to an exempt purpose, either by an express provision in its governing instrument or by operation of law. Reg. 1.501(c)(3)-1(b)(4).
- 3) The Term "articles" includes "the trust instrument, the corporate charter, the articles of association, or any other written instrument by which an organization is created." Reg. 1.501(c)(3)-1(b)(2).

Operational Test

The EO did not satisfy the Operational Test. The EO did not operate exclusively for one or more of the charitable or educational purposes. The EO served a private benefit rather than public interests. EO failed the operational test during the year under examination.

During the year under examination two activities were found to be performed by the EO.

- Rent of office space to for-profit businesses.
- Provide Scholarships to High School Students going to college in Real Estate and related fields.

The EO's income was coming from the rental activity in the amount of XX,XXX and donations in the amount of XX. The scholarship distributions were X,XXX.

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 7 of 14
Name of Taxpayer		Year Ended December 31, 20XX

The EO's rental of its facilities was not an exempt activity, but the issuing of scholarships to high school students going to college was. The rental activity was the EO's primary activity. According to this analysis, the Operational Test was not satisfied.

1) To satisfy the operational test, an organization must be operated exclusively for one or more of the following purposes:

- Religious
- Charitable
- Scientific
- Testing for public safety
- Literary educational
- Fostering national or international sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment)
- Prevention of cruelty to children or animals

Reg. 1.501(c)(3)-1(c)(1) provide that an organization is operated exclusively for charitable purposes only if it engages primarily in activities that accomplish those purposes in (1) above. It is not so operated if more than an insubstantial part of its activities do not further those purposes.

Exempt Activities

The Form 990 described the most significant activities as been exclusively for public, charitable and educational purposes.

During the interview the Bookkeeper said that the primary activity of the organization was to provide scholarships to high school students pursuing a college degree in real estate and related fields. She said that the secondary activities were seminars to teach the elderly in how to do a will and a power of attorney. She added that there was training for realtors.

The EO had some exempt activity, the distribution of scholarships. The books and records showed scholarships and donations, but no other activities, exempt in nature, were found. The educational scholarships were awarded to high school students. The Criteria was for the student to be in the upper XXth to XXth percentile of their class (Not Top XX%). No other exempt activity was found during the audit for the year under examination.

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 8 of 14
Name of Taxpayer		Year Ended December 31, 20XX

The Profit & Loss Statement showed the organization's income and expenses as follows:

<u>Profit & Loss</u>		
Ordinary Income/Expenses	<u>Jan-Dec 20xx</u>	<u>Jan-Aug 20xx</u>
Income		
Rental Income	X	X
Donation Income	X	X
Total Income	X	X
Gross Profit	X	X
Expense		
Maintenance & Repairs	X	X
Miscellaneous	X	X
Personal Property Tax	X	X
Awards	X	X
Bank Service Charges	X	X
Donations	X	X
Education Committee	X	X
Insurance	X	X
Interest Expense	X	X
Janitorial	X	X
Legal and Accounting	X	X
Depreciation Expense	X	X
Scholarship	X	X
Total Expense	X	X
Net Ordinary Income	X	X
Net Income	X	X

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 9 of 14
Name of Taxpayer		Year Ended December 31, 20XX

The analysis of the P&L statement shows that most of its income was coming from rental income. It also shows that XX% of the yearly income went to the Scholarships.

The rental income was an unrelated business activity, of commercial business in kind, and it was not in furtherance of a charitable, educational, etc., purpose as the organization had stated in its organizational documents and Form 1023.

Unlike Private benefit, unrelated trade or business does not normally jeopardize exempt status unless it rises to the level of questioning whether the organization is operated primarily for commercial or exempt purposes. As long it is primarily engaged in related activities, the organization's only consequence is a tax liability of its unrelated business income as imposed by IRC Section 511. On the other hand, private benefit can result in revocation regardless of its insubstantiality.

EO's Final Return

The EO filed a Final Return, Form 990, for the year beginning 01-01-20XX and ending 08-31-20XX. The return was dated 06-20-20XX.

The EO attached to the Form 990 for the year 20XX a "Statement Filed Pursuant to Treasure Regulation Section 1.368-3(a)." The Statement provides the names and EIN's of parties of reorganization. The parties were

The EO terminated on August 31, 20XX, according to a "Plan of Merger" document attached to the Form 990, dated August 15, 20XX. The Plan of merger was by and between ("Acquired Corporation"), a non-profit corporation incorporated under the laws of the State of , and ("Surviving Corporation"), a non-profit corporation incorporated under the laws of the state of .

Schedule "N" of the Form 990, 20XX12 showed the merger as "All assets of the company were transferred pursuant to a tax free merger." The date of the distribution was 08-15-20XX; the Fair market value of asset(s) distributed or amount of transaction expenses was \$XXX,XXX. The Method of determining FMV for asset (s) distributed or transaction expenses was "Book Value". The Name of the recipient was

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 10 of 14
Name of Taxpayer		Year Ended December 31, 20XX

During the interview, the POA stated that the EO had been advised by one of its Firm's former CPA on the Merger of the organizations by a "Tax Free Merger". It was further found that the organization receiving the assets in the merger was a for-profit organization. The POA was asked on this regards and he said that in fact it was a for profit corporation.

LAW:

Section 501(c)(3) of the Code exempts from federal income tax organizations organized and operated exclusively for religious, charitable, scientific, and other exempt purposes, provided that no part of the organization's net earnings inures to the benefit of any private shareholder or individual.

Section 1.501 (a)-1(c) of the regulations defines the words "private shareholder or individual". The words private shareholder or individual in section 501 refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c) (3)-1(d) (1) (i) states that an organization may be exempt as an organization described in section 501(c) (3) if it is organized and operated exclusively for one or more of the following purposes:

- (a) Religious,
- (b) Charitable,
- (c) Scientific,
- (d) Testing for public safety,
- (e) Literary,
- (f) Educational, or
- (g) Prevention of cruelty to children or animals.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, it is necessary for an organization to establish that it is not organized or operated for the

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 11 of 14
Name of Taxpayer		Year Ended December 31, 20XX

benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that in order to be exempt as an organization described in section 501(c)(3) of the Code, the organization must be one that is both organized and operated exclusively for one or more of the purposes specified in that section. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501(c)(3)-1(c) of the regulations specifies that with regard to the primary activities within the operational test, an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will not be regarded as operated exclusively for exempt purposes if more than an insubstantial part of its activities is not in furtherance of exempt purposes.

Section 1.501(c)(3)-1(c)(2) entitled distribution of earnings, provided that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. For the definition of the words "private shareholder or individual", see paragraph (c) of §1.501(a)-1.

Section 1.6001-1(c) of the regulations requires that an exempt organization must maintain records sufficient to demonstrate that it is entitled to tax exempt status.

Section 1.6033-2(h)(2) of the regulations holds that an organization which is exempt from tax, whether or not it is required to file an annual information return, shall submit such additional information as may be required by the Internal Revenue Service for the purpose of inquiring into its exempt status.

In **Bubbling Well Church of Universal Love, Inc. v. Commissioner**, the tax court held that "where the creators control the affairs of the organization, there is an obvious opportunity for abuse, which necessitates an open and candid disclosure of all facts bearing upon the organization, operations, and finances so that the Court can be assured that by granting the claimed exemption it is not sanctioning the abuse of the revenue laws." Implicit in this determination is that the taxpayer has a responsibility to show through its "candid disclosure" of its activities and operations that it continues to qualify for exemption. The "Bubbling Well" opinion goes on to say that if such disclosure is not forthcoming, the

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 12 of 14
Name of Taxpayer		Year Ended December 31, 20XX

logical inference is that the facts, if disclosed, would show that the organization fails to meet the requirements of 501(c)(3).

Rev. Rul. 72-369 states, in part, that in order for an organization to pass the operational test the organization's resources must be devoted to purposes that qualify as exclusively charitable.

Section 508 of the Code provides Special Rules with respect to Section 501(c)(3) organizations.

Section 508(a)(1) of the code provides, with certain exceptions, that an organization organized after October 9, 1969, shall not be treated as an organization described in section 501(c)(3) unless it has given notice to the Secretary or his delegate that it is applying for recognition of such status. If the notice is given after the time prescribed in the *regulations*, section 508(a)(2) provides that the organization shall not be treated as an organization described in section 501(c)(3) for any period before the giving of such notice.

Section 1.508-1(a)(2) (i) of the Income Tax Regulations provides that the required notice is filed by the submission of a properly completed and executed Form 1023 with 15 months from the end of the month in which the organization was organized.

Section 509(a)(2) of the Code specifies these type of organizations are supported primarily by exempt function income. Exempt function income is described as funds derived from an activity which is not an unrelated trade or business. This code section excludes from private foundation classification those **publicly supported organizations that received more than one-third of support** from gifts, grants, contributions, membership fees, and certain gross receipts but **not more than one-third** from gross investment income and **net unrelated business taxable income**.

Rev. Rul. 67-390 states that an exempt unincorporated organization or association and/or trust that incorporates and continues the operations which had qualified it for the exemption, must file an application for exemption to establish that the new entity qualifies for exemption under the Code and applicable regulations. When you create a corporation, even though it may be conducting the same activities and providing the same services as the unincorporated organization, you have created a new entity. Based on this Revenue Ruling, the organization must file an application for exemption to establish that the new entity qualifies for exemption under the Code and applicable regulations.

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 13 of 14
Name of Taxpayer		Year Ended December 31, 20XX

GOVERNMENT'S POSITION:

It is the government's position that _____ did not qualify for exemption under IRC Section 501(c)(3) for the year ended 12-31-20XX, and therefore its tax exempt status should be revoked for the following reasons:

- The organization was not a 501(c)(3) further described in IRC Section 509(a)(2) as it failed the Public Support Test.
- The organization was not a 501(c)(3) as it failed the Operational Test.
- The EO did not operate exclusively for exempt purposes as required by IRC Section 501(c)(3). The EO's unrelated business activity was more than an insubstantial part of its activities. The organization was operated primarily for commercial purposes. It was not primarily engaged in exempt related activities.
- After incorporation in 19XX, the EO did not resubmit to the IRS Form 1023 for exemption under Section 501(c)(3), as per Section 1.508-1(a)(2) of the Income Tax Regulations.
- The EO's assets were transferred to a for-profit organization. According to the EO's Trust and By-laws, the organization, if terminated, would dedicate its assets to a charitable organization. The EO violated the 501(c)(3) rules, the Declaration of Trust and its By-laws. The organization served a private benefit rather than public interests.

Based on the foregoing, EO did not qualify for exemption under IRC Section 501(c)(3) and the regulations, and therefore its tax exempt status should be revoked effective January 1, 20XX.

TAXPAYER'S POSITION:

The _____ indicated that the exempt organization had been terminated and the EO's assets had been transferred to another corporation through a "Tax Free Merger."

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 14 of 14
Name of Taxpayer		Year Ended December 31, 20XX

CONCLUSION:

After reviewing all the facts, law, and positions of the parties involved, we are proposing revocation of the 501(c)(3) exempt status effective **January 1, 20XX.**

The EO did not qualify for exempt status for the year under examination and was not operated exclusively for charitable purposes within the meaning of IRC Section 501(c)(3), further described under Section 509(a)(2).

Forms 1120, *U.S. Corporation Income Tax Return*, should be filed for years 20XX and 20XX, and each year thereafter as long as the organization remains subject to Federal Income Tax.